



Electronic Money: An Update on UK Regulation

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Introduction - my themes today



- Developments in e-money regulation since last April
- e-money is now a regulated activity.....
.....but the perimeter is still being defined
- Dynamic product.....
.....regulators will always be one step behind the market
- The FSA's Regulatory Philosophy
- The FSMA is actually an enlightened piece of legislation

Definition of e-money (UK version):



Electronic money means monetary value as represented by a claim on the issuer which is:

- Stored on an electronic device;
- Issued on receipt of funds; and
- Accepted as a means of payment by persons other than the issuer.

Types of e-money issuer:



- Authorised electronic money institution (ELMI)
- Certified small issuer
- Bank (Credit Institution)

Implementation of e-money directive – part one



- FSMA 2000 (Regulated Activities) (Amendment) Order 2002:
 - defines e-money.
 - adds e-money to list of regulated activities in the UK.
 - incorporates the waiver (for small issuers) into UK law.
- Took effect on 27 April 2002
- Look at HMSO website (www.hmso.gov.uk) under Legislation/UK/Statutory Instruments/2002 No 682

Implementation of e-money directive – part two



- FSA Handbook of Rules and Guidance
 - ELM sourcebook
 - Appendix 3 to AUTH sourcebook (“perimeter guidance”)
- Handbook does not apply to waived issuers
- To be found at our website (www.fsa.gov.uk) then FSA Handbook
- This regime also took effect from 27 April 2002

The European Angle



- UK first to implement in Europe
- Formal meetings of European e-money supervisors.....
.....(16/12/02 and 10/03/03)
- Frequent informal consultations by phone/e-mail
- Need to ensure level regulatory playing field in Europe
- Europe EEA (ie 15 EU MS plus Norway, Iceland and Liechtenstein)
- Many other European countries are looking to build on the FSA regime
- Without further legislation, it is important to adopt pragmatism

Few issuers in the UK so far:



- Single acceptors are excluded (canteen cash cards)
- Two full licences
- Two banks
- Eight small e-money issuers

Second FSA e-money consultation paper (CP 172)



- Published 27 February 2003
- Consultation closes 30 May 2003
- To be followed by Policy Statement in due course (July or September?)
- Groundbreaking approach:
attempts to deal with technology not contemplated by the Directive
- Has sparked off much interest in Europe.

Summary of issues involved in CP 172



- ⌘ e-money, prepaid airtime and Premium Rate Services
- ⌘ e-money and electronic travellers cheques
- ⌘ trust arrangements

E-Money, prepaid airtime and Premium Rate Services (PRS)



- Focuses on PRS as currently marketed by telcos
- Accessed mainly from prepaid mobiles.....
.....but also accessed from landlines using phone cards
- ICSTIS limits PRS to calls providing services costing less than £20
- Who is accepting the prepaid balance as a means of payment?

E-money, prepaid airtime and Premium Rate Services (PRS)



- FSA will follow the flow of payments – if telco is merely a conduit for channelling payments from subscriber to third party PRS provider, this arrangement is likely to involve e-money BUT
- Using prepaid airtime to call PRS numbers is not a use of e-money if:
 - The supply of telecoms services by the mobile airtime provider and the supply of services by the PRS provider can be seen as a single service AND
 - The supply of the airtime and the supply of the PRS take place in the same action.

e-money and travellers cheques



- Electronic travellers' cheques are smartcards carrying a prepaid balance
- Smartcard travellers' cheques are not electronic money if they can only be used at ATMs owned by their issuer
- Using smartcard travellers cheques to purchase:
 - currency at other banks' ATMs or
 - goods or services in shops, hotels and restaurants.....
.....could well be electronic money.

Trust Arrangements



Placing the e-money float in a trust account.....

.....does not prevent the issuer.....

.....from meeting the pre-conditions for issuing e-money

Summary of issues not involved in CP 172



- e-money and transport smartcards – coming later
- Segregation of functions on mobile devices
- Two purses so as to keep prepaid airtime separate from e-money?
- Two classes of mobile device customers?
- - - - - all very difficult!
- Further consultation in due course.....your views welcome

The FSA's Regulatory Objectives:



- Market Confidence
- Public Awareness
- Protection of Consumers
- Reduction of Financial Crime

Market Confidence



- This means maintaining confidence in the UK financial system
- “Financial system” includes both markets/exchanges and regulated activities like issuing e-money
- Regulating the issuers should encourage people to start using e-money
- This should encourage more e-money firms to establish in the UK
- But the negative is failure or fraud in unregulated businesses
- Is this a “price worth paying” to encourage innovation?

Public Awareness



- This means promoting public understanding of e-money
- It includes awareness of benefits and risks involved in using e-money
- It also includes provision of appropriate information/advice on e-money
- FSA believes that "forewarned is forearmed".
- Educating the public about the risks and opportunities thrown up by e-money should lead consumers to behave more rationally
- FSA consumer website aims to contain relevant messages

Protection of Consumers



- This means securing the appropriate degree of protection, having regard to:
 - the risks inherent in e-money
 - the experience/expertise of individuals using e-money
 - consumers' need for advice/information about a new product and
 - the general principle that consumers should take responsibility for their own decisions.
- Consumer protection is achieved through prudential rules.....
.....as well as through detailed conduct of business standards.

Reduction of financial crime



- This means reducing the extent to which it is possible for an authorised firm to be used for a purpose connected with financial crime.
- Difficult to use UK banking system for criminal purposes
- e-money may be attractive to money launderers but danger of detection probably makes it too risky
- Small issuers offer limited scope for serious criminal activity (?)

BUT WE SHALL REMAIN VIGILANT

Section 2 of FSMA makes FSA "have regard to" seven matters:-



- Efficient and economical use of resources
- Responsibilities of managers
- **Regulation should be proportionate**
- **Facilitating innovation**
- **Maintaining a competitive international position for UK**
- Minimise adverse effects of our actions on competition
- Desirability of facilitating competition among those we regulate

The FSA regards e-money as a possible means of:



- extending consumer choice
- providing competition to credit cards and conventional bank accounts
- offering a more convenient and secure means of making payments
- creating an ideal currency for doing business over the Internet or telephone networks
- appealing to the young and technologically literate

The FSA approach is proportionate and risk focused



- We believe e-money poses limited risk to our statutory objectives
- Hence our preference is for a light touch regime
- But this could change where we see consumers being threatened or the potential for financial crime emerging
- It is much easier for us to tailor our regime to the emerging risks of e-money when we can clearly understand what those risks are
- Taking a risk-averse approach from the start could lead us to stifle the new phenomenon at birth.

Conclusions: thoughts I should like to leave with you



1. We believe that a sensible and proportionate system of regulation can assist the development of e-money
2. Regulation should not inhibit good businesses: it should empower them.
3. We believe in open Government – full and free consultation
4. We aspire to be a proactive organisation – not a sleepy, fuddy duddy bureaucracy.